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## **HOUSING ECONOMISTS EXPECT MARKET TURNAROUND TO BEGIN IN 2008**

[Normal View](#)

**October 26, 2007** - Though there appears to be no let-up to the current housing downswing, economists participating in the National Association of Home Builders Fall Construction Forecast Conference on Oct. 24 said they expect the industry to bottom out and to start turning around in 2008.

Acknowledging that there is definitely downward momentum in the market at this time, with starts, sales, prices and permits off, and problems in the subprime and Alt-A mortgage markets, NAHB Chief Economist David Seiders said that housing should nevertheless begin a modest recovery next year.

Despite the present market contraction, Seiders said that housing should begin to turn around next year for a number of reasons: the overall economy and job growth continue to move ahead at a decent pace, core inflation is under control, the late-summer credit crunch in mortgage markets is showing signs of easing since the Federal Reserve cut short-term interest rates on September 18, and the supply-demand equation will be better balanced as builders begin to whittle down excess inventories.

He also noted that the evolving inflation picture gives the central bank latitude to enact more monetary stimulus to support the economy if conditions warrant. Seiders is predicting that the Fed will cut short-term interest rates by another quarter of a percentage point when members of the Federal Open Market Committee meet on October 31 and will enact a similar rate cut by year-end, bringing the federal funds rate down from the current 4.75 percent to 4.25 percent.

With the housing sector facing a large backlog of unsold inventory, Seiders said that starts and permits won't begin to move forward until sales firm up.

"Home sales should bottom out by the end of the first quarter of 2008, and I have starts up in the third quarter of next year, assuming the inventory overhang stabilizes," he said.

Residential fixed investment, which Seiders said could lop off as much as 0.8 percent in Gross Domestic Product (GDP) growth this year, should stop acting as a drag on the economy and turn positive in the fourth quarter of 2008, he added.

NAHB is forecasting 828,000 new single-family home sales for 2007 and 781,000 next year, a 5.6 percent decline. Seiders noted that the peak-to-trough decline in home sales from the boom years of 2003-2005 is more than 40 percent, and as sales begin to move slowly upward beginning in the second quarter of next year, they will still only be on par with levels recorded in the late 1990s.

Total housing starts are expected to register 1.363 million in 2007 and 1.2 million next year, an 11.9 percent decline according to NAHB projections. Single-family starts, Seiders said, are expected to show a 50 percent decline from their peak in the first quarter of 2006 to a trough in next year's second quarter.

Seiders' short-term forecast is based on several assumptions: skillful management of monetary policy by the Federal Reserve, maintenance of solid growth in personal income and employment, a manageable wave of home mortgage foreclosures and better performance of mortgage markets going forward.

However, he observed that the long-term potential for housing activity is very good. "By the end of 2009, we may be at a pace of 1.5 million units of new housing production (including manufactured homes). Once we are out of the woods, we should see good growth in front of us – maybe 2 million per year."

Agreeing that the housing market trough is in sight, Maury Harris, managing director and chief economist at UBS Investment Bank, said that he sees "housing bottoming out in the first half of 2008 and starting to pick up in the second half of the year."

The last time a housing recession was this serious was in the mid-1960s, Harris said, but the big difference between then and now is that "the Fed is not dealing with inflation."

Like Seiders, he sees the federal funds rate dropping to 4.25 percent by year-end and holding steady through 2008.

In forecasting total housing starts of 1.37 million this year and 1.24 million in 2008, Harris said that the housing recovery will be hampered by what he says will be 500,000 foreclosures on subprime and Alt-A loans both this year and next.

"The foreclosures aggravate the inventory situation and weigh on the market more than in past cycles," he said.

Taking what he characterized as a "less negative" spin on the housing market, Michael Moran, chief economist of Daiwa Securities America Inc., said that most of the reporting in the media is "exaggerated" and "sensationalized."

Specifically, he cited the subprime mortgage arena, which makes up 13.5 percent of the market, as opposed to prime lending, which constitutes a 75 percent market share.

"Twenty percent of the subprime market is under stress," said Moran. "Twenty percent of 13 percent is less than 3 percent of the total mortgage market. The economy should absorb this shock."

Commenting on the huge run-up in home prices that occurred in many housing markets between 2000 and 2005, Moran characterized the current home price adjustment as "not especially alarming."

"We are seeing a gradual correction in home prices," he said. "So far, in my view, housing prices are holding up reasonably well."

As for the high number of foreclosures expected this year and next, Moran said the economic fallout will not be as severe as many analysts anticipate because the vast majority of the affected home owners made little or no downpayment on their houses and will walk away without much of a loss.

"The big financial institutions will absorb these losses, but they have the capital to do it," he said.

Moran forecast that housing starts would bottom out in the third quarter of 2008 at a rate of 1.25 million units.

On the inflation front, Moran believes the outlook "looks pretty good" and that the nation's central bank has sufficient leeway to cut rates again, "but not dramatically. The Fed won't adjust monetary policy to rescue the housing market. It will take a macroeconomic outlook."

Predicting that consumer spending will hold up as job and income growth remain positive, all of the panelists pegged the odds of a recession within the next 12 months at between 30 percent and 40 percent.

"The real driving force in personal spending is net worth in the consumer sector, not home equity," said Moran. "Consumers won't back away because household balance sheets are in good shape."

## **The Regional View**

From a regional point of view, Arizona, California, Florida, Nevada and the broader Boston and Washington, D.C. metro areas will be most affected by the negative economic fallout from the subprime mortgage crisis, according to Mark Zandi, chief economist at Moody's Economy.com. Also affected will be areas along the New Jersey coast, the Carolinas, and parts of the industrial Midwest.

Regional economies in these areas, he predicted, will encounter more severe declines in construction and housing prices along with weaker consumer spending and significant job losses in housing-related businesses than other markets across the country.

Places that are experiencing the most significant weakening of economic activity at present include Phoenix, parts of central and southern California, Las Vegas and Reno, Nevada, as well as parts of Florida's east and west coasts, said Zandi. He expects housing activity in these areas to bottom out in late 2008 "at best."

Bernard Markstein, NAHB's Director of Forecasting, put today's housing picture into greater historical context. Explaining that although year-over-year numbers for home prices and production are indeed expected to show substantial declines while the downturn continues, he noted that last year's housing statistics (which were clearly unsustainable) are not the ideal comparison for current activity. If instead, for example, you were to compare anticipated starts activity to the 2002-2003 levels that offer a more "normal" benchmark, you would not have to look too far down the road to see a return to equilibrium in 2008-2009.

Markstein agreed that the biggest house-price declines will be relatively localized in the California, Florida, Nevada, upper Northeast and Midwest markets, but he also pointed out that in quite a few housing markets, prices are still rising. Whether you consider this good news or bad, he said, it's a far different story than what most people have gleaned from the media headlines. In fact, with just a few notable exceptions, most of the country's metropolitan statistical areas have recorded little or no decline in house prices between their recent peaks and the second quarter of 2007. The bottom line is that, while rapid price gains are a thing of the past, a lot of home owners are "still in good shape" with regard to their home values.